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How Solid is the Surplus?

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Part I: The Big Picture

Introduction

Next year, for the first time in forty years, the federal government will achieve a budget surplus without relying on the surplus in Social Security. This achievement results from difficult budget decisions made over the past decade. Budget surpluses are projected to extend well into the future, and these too depend on difficult choices. In fact, the large surpluses that OMB and CBO are both projecting assume significant reductions in appropriations — cuts that run deeper than any Congress has ever imposed. To the extent such spending cuts are not made, the surplus available for tax cuts or other purposes will be smaller.

This paper attempts to lay out choices. It clarifies the assumptions about spending that underlie the surplus projections and the long-term implications of abiding by these assumptions.

Living Within the Caps

CBO projects a non-Social Security surplus totaling $964 billion over the next ten years.[1] This projection assumes that appropriations will be capped at designated levels in 2000, 2001, and 2002, in accordance with the Balanced Budget Act of 1997. Thereafter, the projected surplus assumes that total appropriations will remain at the 2002 funding level in real purchasing power, with nominal spending growing at the rate of inflation. In addition, the projections assume that there will be no emergencies in the next decade that require federal spending. These assumptions and the surplus that results from them are referred to as the "capped baseline."

Table 1 shows the implications over the next ten years of sticking with the caps. It gives the change in real purchasing power for three categories of appropriations: defense, highways and mass transit, and all other appropriated spending. It focuses on real purchasing power because this represents the extent to which programs either contract or expand. After all, if prices rise but program funding is constant in dollar terms, then fewer real goods and services are available to pursue the program's objectives.

[1] CBO's published figure for the non-Social-Security budget surplus is $996 billion, but that figure excludes $31 billion in Social Security administrative costs which Congress includes in the non-Social-Security budget because they are subject to the statutory caps on appropriated programs. For congressional purposes, therefore, CBO's estimated surpluses total $964 billion.

Table 1: 10-Year Reductions in Purchasing Power Implied by Adhering to The Caps

Outlays for appropriated programs, FY 2000 - FY 2009, in billions of dollars

	Defense	Highways / mass transit	All other appropriated programs	All appropriated programs
If the reductions are taken across the board...	-277	-30	-288	-595
If defense follows the President's path and transportation follows TEA21...............	150	4	-749	-595

The table shows that if all appropriations accounts share equally in the cuts relative to inflation, then defense spending over the next ten years is $277 billion below what is necessary to maintain the same real program level as in 1999, excluding the unprecedented $34 billion in "emergency" spending that year. Similarly, the purchasing power of highway programs is reduced $30 billion below a constant inflation-adjusted 1999 level, and other appropriations are $288 billion lower.

However, there already has been a commitment to increase highway and mass transit spending over the next several years, and there is bipartisan support for raising defense spending. Thus, the table also shows the effect of assuming that the legislated increase in transportation spending (TEA21) is not reversed and that the President's requested increase in defense spending is enacted. In that case, other appropriated accounts over the next ten years will have to be $749 billion below the levels needed to maintain 1999 purchasing power.

Table 2 shows where sticking with the appropriations caps would leave us in 2009. It shows the percentage cuts from constant 1999 purchasing power needed to stay within the spending caps. Again, it illustrates the deeper cuts required in other appropriations if defense and transportation spending is to be increased. In this case, other appropriations would have to be reduced 31 percent from their 1999 level, after adjusting for inflation.

Table 2: FY 2009 Percentage Reduction in Purchasing Power Implied by Adhering to The Caps

	Defense	Highways / mass transit	All other appropriated programs	All appropriated programs
If the reductions are taken across the board...	-10%	-10%	-10%	-10%
If defense follows the President's path and transportation follows TEA21................	10%	4%	-31%	-10%

Table 3 shows the same information for 2009, but this time expressed in dollar terms. If Congress follows through on defense and transportation commitments, all other appropriations will have to be cut by $112 billion in 2009. In terms of funding levels, inflation-adjusted spending for other appropriations would have to be reduced from $365.4 billion to $253.6 billion.

Table 3: FY 2009 Reduction in Purchasing Power Implied by Adhering to The Caps

Outlays for appropriated programs in FY 2009, in billions of dollars

	Defense	Highways / mass transit	All other appropriated programs	All appropriated programs
If the reductions are taken across the board...	-35	-4	-37	-75
If defense follows the President's path and transportation follows TEA21................	35	1	-112	-75

A $112 billion cut in other appropriations would require a significant reorientation of many basic government functions. This part of the federal budget is composed of hundreds of programs, each of whose individual cost is small relative to the size of the cut needed to stay within the caps.

To cut other appropriations by this amount while increasing defense and transportation funding would be hard to achieve solely by eliminating waste. Whole programs presumably would have to be eliminated rather than downsized. The table below provides an illustrative list of some of the high-profile items in this category and the 2009 funding levels needed to maintain constant purchasing power at the 1999 level.

Table 4: 2009 Baseline Funding for Selected Programs
(dollars in billions)

Veterans' hospitals and medical care	24.5
National Institutes of Health (NIH)	18.8
NASA	17.2
Internal Revenue Service	11.0
FAA national air traffic control system	10.2
Education for the disadvantaged (Title I)	10.1
Special education	6.6
Community Development Block Grants	5.8
Head Start	5.7
EPA Superfund Program and grants to states	5.6
WIC (nutrition for women, infants, and children)	4.8
National Science Foundation (NSF)	4.5
Federal Bureau of Investigation (FBI)	3.4
Coast Guard, operating expenses	3.2
Customs	2.3
Immigration and Naturalization Service	2.3
National Park Service	1.8
Drug Enforcement Administration	1.1
FEMA	0.9
Federal capital grants for Amtrak	0.7
TOTAL	**$140.5**

Preserving all these items will require $140.5 billion in funding. If these appropriations are considered off-limits and the increases for defense and transportation also are off-limits, then all other appropriations must be cut by 50 percent to stay within the caps. This means sharp and politically unacceptable cuts for other programs like the Food and Drug Administration, Pell Grants, the National Weather Service, wildfire management, agricultural conservation, flood control, Section 8 housing, and teacher training.

Circumventing the Caps

Because of the evident difficulty in making the cuts needed to stay within the caps, some have questioned whether the projected surpluses will materialize. As described below, they note that

Congress failed last year to stay within the 1999 cap and appears to be having difficulty meeting the 2000 target as well. They argue that a growing population, an increasingly complex economy, and the responsibility of being the world's only superpower will inevitably lead to higher appropriations than assumed in the budget baseline.

Of course, more funding for appropriations comes at the cost of a reduced non-Social Security surplus. As noted at the beginning, this implies that there would be less money to devote to tax cuts or domestic programs. The table below illustrates just how quickly the projected surplus would evaporate if Congress provides constant purchasing power for appropriations over the next decade.

Table 5: Appropriated Programs and the Projected Surplus: FY 2000-09
(ten-year outlay totals in billions of dollars)

CBO extrapolation of surplus, excluding Social Security	964
Minus:	
Funding needed to maintain 1999 purchasing power, excluding all 1999 emergencies	595
Average emergency costs[2]	90
Additional federal interest expenses	179
Equals:	
Remaining surplus	100

If total appropriations funding is held constant at 1999's level of purchasing power, $595 billion of the ten-year projected surplus is consumed (as was also shown above in Table 1). Of course, even if total inflation-adjusted appropriations are held constant, increased defense and transportation spending would necessitate cuts for other appropriations.

CBO's baseline projections assume no future emergencies, but it is not realistic to expect that we will suffer no earthquakes, hurricanes, droughts, or military emergencies over the next decade. Therefore, Table 5 also shows a $90-billion reduction of the surplus for emergencies. This equals the average cost of emergencies from 1991 through 1998, excluding the Gulf War.[3]

These two claims on the surplus have an impact on the very sizeable decline in debt service built into the CBO baseline. The additional funding needed to keep appropriations' purchasing power constant and to provide for emergencies means that less public debt will be repaid than CBO assumes. As a consequence, the reduction in government interest payments will be $179 billion smaller than the reduction assumed by CBO.

[2]This figure is based on the average costs of emergencies in 1991 through 1998, excluding costs of the Gulf War. Like the non-emergency appropriations, these amounts are adjusted only to keep pace with inflation.

[3]Nowhere, though, does the table include the unprecedented $34 billion in 1999 "emergency" spending that included many non-emergency items.

Together, these adjustments reduce the ten-year, $964 billion non-Social-Security surplus by 90 percent. The remaining $100 billion doesn't even come close to providing enough money for all the uses that have been proposed. Clearly, tax cuts of $864 billion are out of the question if one believes that the appropriations cuts assumed in the budget baseline will not be enacted.

Part II: 1999 and the Caps

Congress did not abide by the spirit of the appropriations spending caps in 1999, using several means. The largest evasion occurred by enacting a total of $34 billion in emergency funding, which automatically raised the 1999 statutory caps.[4] Emergencies normally refer to unforeseen occurrences, such as war or natural disasters, that warrant an immediate response (and therefore immediate funding) from the federal government. While this analysis does not attempt to examine all items that comprise the $34 billion in emergency funding, there were clear examples of items that were labeled emergencies even though they represented ongoing programs. For example, $1 billion was added for ongoing ballistic missile defense research and development programs. Also, emergency funding was included for agencies such as the Tennessee Valley Authority and Americorps. Emergency appropriations for 1999 were more than four times the annual average for emergencies (not including Operation Desert Shield-Desert Storm) in the 1990s.

Congress also used more arcane means to avoid the cuts required by the 1999 caps. First, Congress enacted changes to mandatory programs in appropriations bills that decreased mandatory spending primarily on a one-time-only basis. An example was the provision requiring the federal government to sell the stock portfolios of certain District of Columbia pension funds and buy Treasury securities instead. Under budget rules, these savings are credited to the Appropriations Committee, which can then "spend" the savings without breaching the caps. There was approximately $4 billion in such credits and subsequent funding for 1999, but many of these credits will be unavailable for 2000.

Second, Congress effectively raised the caps by $15.4 billion between 1999 and 2002 when it enacted the Transportation Equity Act for the 21st Century (TEA-21). TEA-21 established two new appropriation categories, Highways and Mass Transit, and increased funding for those two areas. As a partial offset, TEA-21 lowered the existing caps for the remaining appropriations, but this reduction was $15.4 billion less than the amount provided for the two new categories.[5]

[4] The $34 billion includes both mandatory and discretionary emergency funding.

[5] In an effort to offset this net increase in appropriated spending, TEA-21 made cuts to veterans' compensation benefits, Title XX, and certain other mandatory programs. However, between 1999-2002, CBO estimates these offsets fall $9.3 billion short of completely offsetting the increased spending in the bill.

Part III: The FY 2000 Appropriations Predicament

Part II described the measures Congress used in order to avoid the budget cuts that would have been required by strict adherence to the 1999 appropriations caps. The caps for 2000 are even tighter, meaning that Congress may very well resort to similar tactics this year. Part III sketches out the severity of cuts required by the 2000 caps and demonstrates the unrealistic nature of the assumptions underlying the projections of huge non-Social Security surpluses.

Commerce-Justice-State

For 2000, the House Republican 302(b) allocation provides $30.5 billion for the Commerce-State-Justice appropriations bill. This level of funding is a cut of 11.2 percent ($3.9 billion) in purchasing power for the programs funded by this bill, including:

- ***Embassy Security —*** An across-the board cut of 11.2 percent would mean a $337 million drop in funding for the operation of the State Department and U.S. embassies. A cut of this magnitude would significantly reduce the security at our overseas facilities and could reverse many of the measures put in place after the terrorist bombings of our embassies in Kenya and Tanzania.

- ***Law Enforcement Agencies —*** For the Federal Bureau of Investigation (FBI), an across-the-board cut of 11.2 percent would mean a decrease of $315 million in purchasing power for salaries and expenses. A cut of this magnitude could result in a reduction of approximately 2,500 FBI agents. A cut of 11.2 percent would lower the Drug Enforcement Agency's purchasing power for salaries and expenses by $142 million. For the DEA, such a large cut could result in a reduction of over 700 agents. A cut of 11.2 percent would mean a loss in purchasing power of $288 million in salaries and expenses for the Immigration and Naturalization Service (INS). For the INS, this huge cut could result in a reduction of over 1,000 border patrol agents.

Labor-HHS-Education

For 2000, the House Republican 302(b) allocation provides $78.1 billion for the appropriations bill funding the Departments of Labor, Health and Human Services, Education, and related agencies. This level of funding is a cut of 13.9 percent ($12.6 billion) in purchasing power for the programs funded by this bill, including:

- ***National Institutes of Health (NIH) —*** For NIH, an across-the-board cut of this magnitude would reverse Congress' intent to double NIH funding by 2003. In 1999, Congress increased NIH's funding by 15 percent over the previous year's increase of seven percent. The 1999 increase is viewed by many as the down payment on a series of promised increases designed to double NIH funding over five years. Applying a cut of 13.9 percent to NIH in 2000 would result in a cut of $2.2 billion in purchasing power. An increase of $2.3 billion over the 1999 level is necessary to stick to the schedule of doubling NIH's funding by 2003.

- ***Education for the Disadvantaged (Title I of the Elementary and Secondary Education Act) —*** An across-the-board cut of 13.9 percent would slash Title I by $1.2 billion, depriving 1.9 million disadvantaged children from services needed to help them succeed in school.

- ***21st Century Community Learning Centers —*** A 13.9 percent cut would reduce funding for this program by $36 million in purchasing power, denying after-school and summer school programs to more than 66,000 children.

- ***Head Start —*** For Head Start, a reduction of this magnitude would cut services to between 35,000 and 60,000 low-income children. The current funding level already falls far short of being able to serve hundreds of thousands of eligible children and families.

VA-HUD-Independent Agencies

For 2000, the House Republican 302(b) allocation provides $66.2 billion for the appropriations bill funding the Departments of Veterans Affairs, Housing and Urban Development, and various independent agencies. This level of funding is a cut of 7.2 percent ($5.2 billion) in purchasing power for the programs funded by this bill, including:

- ***Low-Income Housing Programs —*** More than three million low-income families currently depend on annual renewal of Section 8 rental assistance either through vouchers or project-based assistance. A reduction of this magnitude would mean about 185,000 fewer households and 450,000 fewer individuals could be served in 2000 than in 1999. Reductions also would cut special housing programs serving the elderly and disabled, the homeless, and persons with AIDS. Also affected would be HUD's housing rehabilitation and production program, which increases the availability of decent, safe, and affordable housing in both urban and rural areas.

- ***Community Development Block Grants (CDBGs) —*** An across-the-board cut of this magnitude would decrease the purchasing power of the CDBG program by $348 million, jeopardizing thousands of local improvement initiatives and cutting assistance to 28,000 homes and support for 44,000 jobs in low-income areas.

- ***Veterans' Health Programs —*** An across-the-board cut of 7.2 percent would mean a $1.4 billion drop in purchasing power for veterans' health programs, which are recognized as already being woefully underfunded. Republicans promised to increase funding for veterans' health care in 2000; if they fulfill this promise, the rest of the programs funded by this appropriations bill will suffer even more. Just maintaining the purchasing power of the veterans' health care programs at the 1999 level would increase the required cut to all other programs in the bill from 7.2 percent to 9.8 percent.
- ***Environmental Assistance for States and Tribes —*** In 1999, EPA is providing $3.4 billion in financial assistance to states and tribes to help them protect public health and the environment. EPA grants bolster state revolving loan funds, which in turn help localities build new drinking water and wastewater treatment plants. Other EPA grants help states and

tribes monitor air quality, teach pollution prevention, and monitor compliance with environmental laws. An across-the-board cut of 7.2 percent in purchasing power would reduce this assistance by $250 million, meaning some communities would have to wait even longer for much-needed improvements to their public health infrastructure.

- ***National Science Foundation* —** For NSF, an across-the-board cut of this magnitude would mean cutting the total number of research grants by over 1,300. Alternatively, NSF could end support for research in selected areas, such as computer and information science and engineering or atmospheric and earth sciences.

General Notes:

- All years are fiscal years unless otherwise noted.
- Numbers may not add due to rounding.
- Funding levels for discretionary programs are stated in budget authority, unless otherwise noted. Funding levels for entitlements and other direct spending programs represent outlays.